

ORIGINAL



0000103850

RECEIVED

FENNEMORE CRAIG, P.C.  
Patrick J. Black (No. 017141)  
3003 North Central Avenue, Suite 2600  
Phoenix, Arizona 85012  
Telephone: (602) 916-5400  
Facsimile: (602) 916-5600  
Email: pblack@fclaw.com

2009 OCT 13 P 4: 39  
AZ CORP COMMISSION  
DOCKET CONTROL

Attorneys for Valley Utilities Water Company

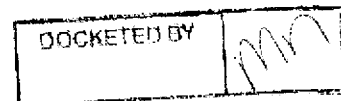
**BEFORE THE ARIZONA CORPORATION COMMISSION**

IN THE MATTER OF THE  
APPLICATION OF VALLEY UTILITIES  
WATER COMPANY, AN ARIZONA  
CORPORATION, FOR A  
DETERMINATION OF THE FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN  
ITS RATES AND CHARGES FOR  
UTILITY SERVICE BASED THEREON.

DOCKET NO: W-01412A-08-0586

Arizona Corporation Commission  
**DOCKETED**

OCT 13 2009



**VALLEY UTILITIES WATER COMPANY'S**

**POST-HEARING BRIEF**

**October 13, 2009**

## INTRODUCTION

Valley Utilities Water Company ("VUWCO" or the "Company") hereby files this Post-Hearing Brief in the above-captioned matter. Throughout the course of this proceeding, VUWCO has worked extensively with Arizona Corporation Commission ("Commission") Staff to successfully reduce the number of disputed issues in this case.

As a result, the Company and Staff agree to the following:

- that the Company has a negative rate base of (\$169,027);
- that the Company is entitled to an annual operating income of approximately \$132,000;
- the Company maintain an operating margin of ten percent (10%)<sup>1</sup>;
- a total annual revenue requirement of approximately \$1,318,714<sup>2</sup>;
- the exclusion of arsenic treatment facilities from the Company's rate base;
- the inclusion of Well No. 6 in rate base as "used and useful" due to its operation and providing service to existing customers;
- an increase in pumping purchased power expense<sup>3</sup>;
- the implementation of policies and procedures that ensure compliance with Commission decisions in the future; and
- that the Company file for approval of its Central Arizona Project ("CAP") Municipal and Industrial Subcontract in the event the Commission determines such approval is necessary.<sup>4</sup>

<sup>1</sup> VUWCO supports a 10% operating margin provided that the Commission adopt the Company's proposed additional revenue annualization downward adjustment of \$102,966. If the adjustment is not adopted, the Company is recommending a 13% operating margin. Rejoinder Testimony of Thomas Bourassa ("Bourassa Rj.") at 5.

<sup>2</sup> Staff proposes an annual revenue requirement of \$1,324,266. However, this figure should change based on revisions adopted by Staff during the hearing, such as lost revenue associated with eliminating the Company's current \$10.00 monthly late fee.

<sup>3</sup> Transcript ("Tr.") at 111-112. Staff's adjustment of \$18,524 is based on not adopting the Company's proposed revenue annualization. The Company's proposed adjustment is \$17,219 based on revenue annualization.

<sup>4</sup> This involves a separate proceeding for another water utility. Tr. at 184-186.

1 Furthermore, because the Commission recently approved the Company's arsenic  
2 remediation surcharge mechanism ("ARSM") application as recommended by Staff in  
3 Decision No. 71287 (October 7, 2009), how to address non-approval is no longer an issue.  
4 There are however a few issues still in dispute between VUWCO and Staff. The primary  
5 disputed issue concerns the parties' respective proposed adjusted test-year revenues,  
6 which in turn affect the overall revenue increase and percentage rate increase. Although  
7 the revenue requirement proposed by the parties is similar, the parties differ on the  
8 amount of revenue increase needed to achieve the final result by approximately \$94,000.<sup>5</sup>

9 There also continues to be a dispute over some other issues, including Staff's  
10 proposal to eliminate and replace the Company's flat late fee of \$10.00 to 1.5% of the  
11 outstanding balance, VUWCO's proposal to reduce interest on security deposits to two  
12 percent (2%), the amount of maintenance and repairs expense resulting from  
13 'normalization', and differences in rate design. These disputed issues are analyzed  
14 below.<sup>6</sup>

## 15 ANALYSIS

### 16 **I. The Company's Proposed Additional Revenue Annualization Downward** 17 **Adjustment of \$102,966 Reflects and "Known and Measurable" Change That,** 18 **If Adopted, Will Obtain a Normal or More Realistic Relationship Between** **Revenues, Expenses and Rate Base for VUWCO.**

19 The Company is proposing a total revenue annualization downward adjustment of  
20 \$127,503 based on actual water sales that occurred for the 12 months after the test-year.  
21 Bourassa Rj. at 5. In dispute is \$102,966 of downward adjustments proposed by the  
22 Company that reflect actual water sales losses. *Id.*, Tr. at 125. Staff opposes this further

23 <sup>5</sup> This figure represents the pre-hearing position of the parties. Staff has not yet filed revised schedules, but during  
24 the hearing agreed to two major adjustments; (1) to purchased power expense, an additional \$18,524, and (2)  
approximately \$23,000 to reflect loss revenue if the \$10 monthly late fee charge is replaced with a 1.5% charge on  
outstanding balances.

25 <sup>6</sup> Because Staff has not yet filed a complete set of revised schedules (Tr. at 184) as of October 13, 2009, VUWCO  
26 reserves the right to amend this Post-Hearing Brief to address any substantive changes in the revised schedules that  
may alter the Company's position.

1 downward adjustment because it is not known and measurable, occurred outside the test-  
2 year and creates a 'mismatch' between revenue and expenses. Surrebuttal Testimony of  
3 Gary T. McMurry ("McMurry Sb.") at 10. However, on cross-examination Staff  
4 conceded that the \$102,966 downward adjustment was based on actual water data, and  
5 that Staff did not have the time to perform a full audit of this data. Tr. at 128.  
6 Furthermore, Staff agreed that the Company proposed matching adjustments to purchased  
7 power and chemical expenses due to reduced water pumping was based on the actual  
8 amount of water pumped during the 12 months after the test-year. Tr. at 126.

9 To support the revenue annualization adjustment, Robert Prince provided  
10 testimony concerning declining water sales due to a lack of construction, a declining  
11 customer base and water conservation efforts based on the Company's current rate design.  
12 Rejoinder Testimony of Robert L. Prince ("Prince Rejoinder") at 2-4; Tr. at 19. On cross-  
13 examination, Mr. Prince conceded that it is impossible to determine when an economic  
14 turnaround might go into effect. Tr. at 31-32. However, this uncertainty should not result  
15 in a reduction in operating revenue that the Company desperately needs in order to  
16 continue providing adequate water service to its customers. And given the state of the  
17 economy and the housing market especially, the prudent approach for the Commission  
18 would be to fashion a more realistic relationship between revenue, expenses and rate base.  
19 Staff suggested that if VUWCO was experiencing insufficient cash flow to pay bills, the  
20 Company could file for emergency rates. Tr. at 33. However, even Staff agrees that  
21 granting emergency rate relief requires a "sudden" change in circumstances to constitute  
22 an emergency, and that a declining customer base and water sales over a two or three-year  
23 period would unlikely be considered a 'sudden' change to warrant interim relief. Tr. at  
24 135.

25 The purpose of the Company's proposed revenue annualization is to obtain a  
26 normal or more realistic relationship between revenue, expenses and rate base. Bourassa

1 Rj. at 4. Staff did not provide any evidence to refute VUWCO's position that actual water  
2 sales occurring within the 12 months after the test-year is more indicative of water sales  
3 the Company is likely to experience over the next few years, especially when compared to  
4 what occurred during the test-year.<sup>7</sup> Even Staff's engineering witness, Marlin Scott,  
5 testified that his customer growth projection was based on a lineal regression analysis, and  
6 was used only to determine the status of the Company's capacity. Tr. at 102.  
7 Furthermore, Mr. Scott concedes that actual data trends show the Company's customer  
8 base is slowly declining. Tr. at 103. If Staff would rather that the Company have extra  
9 capacity instead of not enough capacity due the detrimental effects on quality of service,  
10 then the same reasoning should apply to revenue, as slightly less revenue rather than more  
11 revenue would result in a reduction in the quality of service VUWCO provides to its  
12 customers.

13 **II. An Interest Rate of Two Percent on Security Deposits Is Reasonable Given**  
14 **Current Market Conditions.**

15 The Company is proposing to revise the amount of interest customers earn on  
16 security deposits from six percent (6.0%) to two percent (2.0%). The reasoning is simple;  
17 a 2% interest rate reflects current market conditions. Bourassa Rj. at 18. During the  
18 hearing, Staff conceded that Mr. Bourassa testimony on current interest rates was  
19 accurate. Tr. at 124. Staff's recommendation of 6% is based on the "default" provision  
20 provided in A.A.C. R14-2-403(b)(3). However, Staff concedes that modifying interest  
21 rates on security deposits – up or down – is something that the Commission should do to  
22 reflect market conditions when they benefits ratepayers as well. Tr. at 139. The  
23 Company does not refute this position, and will propose interest rates on security deposits

24 <sup>7</sup> Staff witness Gary McMurry testified that he was not able to audit the water sales data for this period that was  
25 provided by the Company, but would have done so if he had enough time. Tr. at 129. The Company is sympathetic  
26 to Mr. McMurry's case load and the pressures put on Commission Staff. However, nearly \$100,000 in lost revenue  
to a company the size of VUWCO would have a substantial detrimental impact on its ability to continue providing  
adequate service to customers, and impair the overall financial viability of the Company.

1 that reflect market conditions when seeking to revise its tariffs. Indeed, A.A.C. R14-2-  
2 403(b)(3) already provides this flexibility to utilities and the Commission. However, the  
3 evidence in this proceeding establishes that the Company's proposed interest rate is more  
4 reasonable given current market conditions than Staff's proposed 6.0%.

5 **III. The Company's Monthly Late Fee Charge of \$10.00 is Reasonable and Should**  
6 **Not Be Replaced By a 1.5% Charge of Outstanding Amounts.**

7 Staff is proposing to modify the Company's monthly late fee charge of \$10.00 per  
8 month to 1.5% of the unpaid balance. Tr. at 113. During the hearing, Staff indicated that  
9 if the recommendation is adopted, a corresponding adjustment to water revenue should be  
10 made to reflect lost revenue. Tr. at 113, 123. Without this revenue adjustment, Staff's  
11 recommended rate increase is understated by over \$24,000. Staff agreed to make this  
12 adjustment and Staff has testified that its final schedules will reflect this additional  
13 adjustment to revenues. *Id.* The Company agrees with the need to make the required  
14 revenue adjustment in the event that the recommendation to adopt a 1.5% late charge on  
15 unpaid balances is approved. However, the Company continues to believe that it is  
16 inappropriate to require those customers who pay their monthly bills on time to make up  
17 the resulting lost revenue in rates for those who are late, in the event the late fee policy is  
18 revised.

19 **IV. The Company's Proposed Rate Design is in the Public Interest and Should Be**  
20 **Adopted.**

21 The Company is proposing a conservation-oriented inverted tier rate design – an  
22 inverted three tier for the smaller residential customers and an inverted two-tier design for  
23 small commercial and larger metered customers. Bourassa Rj. at 12-17. This design is  
24 similar to the rate design adopted in the Company's last case and this rate design has  
25 arguably resulted in water conservation from the last test year to the current test year. *Id.*  
26 at 14. The modification to the current rate design that Mr. Bourassa recommends is to

1 lower the break-over points of the larger meters by setting the break-over points relative to  
2 the flows of a 5/8 inch meter. Absent a cost of service study, setting the break-over points  
3 on the relative flows of a 5/8 inch meter makes the most sense. Tr. at 81-82. Mr.  
4 Bourassa believes that further conservation will be achieved by the Company's  
5 recommended lower break-over points for the larger meters. Bourassa Rj. at 16-17; Tr. at  
6 81-82.

7 The rate design proposed by the Company applies the rate increase evenly across  
8 all monthly minimums and commodity rates. The differential between the commodity  
9 rates under the Company's design is consistent with the previously authorized commodity  
10 rates. The Company has criticized Staff's break-over points and commodity rates.  
11 Staff's break-over points are not scaled on the flows of a 5/8 inch meter. Staff has not  
12 explained how it set the break-over points. In addition, Staff's rate design shifts revenue  
13 recovery from the smaller residential customers to the larger metered commercial  
14 customers to a much greater extent than the Company's rate design. Bourassa Rb. at 19,  
15 Bourassa Rj. at 18; Tr. at 83-84. Absent a cost of service study, the rate design should not  
16 significantly shift revenues from one class of customer to another. Tr. at 84. As Mr.  
17 Bourassa testified, cost of service studies show the larger metered customer pay more than  
18 their cost of service and thereby subsidize the smaller metered customers. *Id.*

19 The Company also proposes to continue a monthly minimum on construction  
20 meters. Staff disagrees. The Company believes that a monthly minimum charge  
21 encourages builders and contractors to return the meters when they are no longer in use.  
22 Bourassa Rj. at 17. The Company currently pays interest on deposits so there is no  
23 incentive for builders/contractors to return the meters when they are no longer receiving  
24 water, which in turn places a demand on the available number of meters for development  
25 purposes.

26 ///

1     **V. MISCELLANEOUS**

2         **A. Purchased Power Expense**

3             Staff has agreed that a purchased power expense adjustment should be made to  
4 reflect known and measurable rate increases from Arizona Public Service Company  
5 (“APS”), the Company’s power provider. The Company proposes an adjustment in its  
6 rebuttal. Bourassa Rb. at 16. Staff’s testified that its final schedules will reflect an  
7 additional adjustment to purchased power expense. Tr. at 111-112. Staff’s adjustment  
8 will be higher (\$18,524) than the Company’s proposed adjustment (\$17,219) since Staff  
9 opposes the Company’s additional revenue annualization adjustment. Bourassa Rb. at 14-  
10 16; Bourassa Rj. at 3-6. In either case, the Company supports an adjustment for  
11 purchased power expenses to reflect the increase in APS rates.

12         **B. Maintenance and Repairs**

13             The Company and Staff disagree on Staff’s normalization of repairs and  
14 maintenance expense. Staff “normalizes” repairs and maintenance by using a three year  
15 historical average, which is \$12,688. The Company is proposing the test-year expense of  
16 \$14,201. The Company has shown that Staff’s normalization adjustment is highly  
17 subjective and if Staff had computed its normalization adjustment using different years,  
18 both historical and future, the resulting “normalized” level of repairs and maintenance  
19 expense would have been higher. Tr. at 133. All of the alternative “normalization”  
20 approaches as set forth by the Company would produce higher levels of expense than  
21 Staff’s recommendation, and two of the approaches produce levels of expense even  
22 greater than the test year level. Bourassa Rb. at 18-19. Because the actual test year  
23 repairs and maintenance expense falls within the ranges of all the normalization approach  
24 estimates, the test year level of expense should remain unchanged.



1           C.     VUWCO Compliance

2           During the hearing, Company witness Robert Prince testified that he agreed with  
3 three of the five non-compliance issues raised by Staff. Tr. at 13. The Company and Staff  
4 subsequently agreed to postpone filing an application for approval of the CAP contract  
5 pending resolution by the Commission in another proceeding. Tr. 184-186. In addition,  
6 the Commission recently issued Decision No. 71287 (October 7, 2009), which addresses  
7 issues related to the Company's use of set-aside monies and produces a level of arsenic  
8 remediation surcharge that reflects the effect of past non-compliance. The Company  
9 agrees with Staff's recommendations concerning the remainder of the non-compliance  
10 issues, and the policies and procedures to be adopted that address same. Tr. at 14-15.

11                               CONCLUSION

12           Although the Company and Staff have resolved many of the disputed issues in this  
13 rate proceeding, it is important to recognize that the remaining disputed issues will  
14 collectively have a major impact on VUWCO's ability to maintain adequate service to its  
15 customers. Of particular importance is the Company's proposed revenue annualization,  
16 which more accurately reflects the relationship between revenue, expenses and rates.  
17 There is no doubt that the utility is feeling the effects of the economic recession though a  
18 reduction of construction meter water sales, a declining customer base and successful  
19 conservation efforts. While remaining VUWCO employees have done their best with a  
20 reduced staff, increased work load and longer hours, sufficient cash-flow and a true  
21 10.00% operating margin will allow the Company to get to more normalized operations  
22 conditions. Adoption of the Company's proposed revenue annualization will allow  
23 VUWCO sufficient cash-flow to maintain operations, and produce equity that the  
24 Company can later reinvest consistent with previous Commission decisions. VUWCO's  
25 proposed resolution to the remaining issues in dispute (as outlined above) will help  
26 maintain a viable water service provider, and approval is therefore in the public interest.

1 RESPECTFULLY DATED this 13<sup>th</sup> day of October, 2009.

2 FENNEMORE CRAIG, P.C.

3  
4 By: 

5 Patrick J. Black  
6 Attorneys for Valley Utilities Water Company

7 **ORIGINAL** and 13 copies of the foregoing filed  
8 this 13<sup>th</sup> day of October, 2009 with:

9 Docket Control  
10 Arizona Corporation Commission  
11 1200 West Washington Street  
12 Phoenix, AZ 85007

13 **COPY** of the foregoing hand-delivered  
14 this 13<sup>th</sup> day of ~~September~~ <sup>October</sup>, 2009 to:

15 Sarah Harpring  
16 Administrative Law Judge  
17 Hearing Division  
18 Arizona Corporation Commission  
19 1200 West Washington Street  
20 Phoenix, AZ 85007

21 Kevin Torrey, Esq.  
22 Legal Division  
23 Arizona Corporation Commission  
24 1200 West Washington Street  
25 Phoenix, AZ 85007

26 Ernest Johnson, Director  
Utilities Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

By: 

2245412.1/24964.003